[JOINT COMMITTEE PRINT]

DESCRIPTION OF S. 1396 (ENERGY SECURITY TAX INCENTIVES ACT OF 1983)

SCHEDULED FOR A HEARING

BEFORE THE

SUBCOMMITTEE ON ENERGY AND AGRICULTURAL TAXATION

OF THE

COMMITTEE ON FINANCE

ON JUNE 17, 1983

PREPARED BY THE STAFF

OF THE

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INTRODUCTION

The Subcommittee on Energy and Agricultural Taxation of the Senate Committee on Finance has scheduled a hearing on June 17, 1983, on S. 1396 ("Energy Security Tax Incentives Act of 1983", introduced by Senators Domenici, Jackson, Wallop, McClure, Byrd, Garn, and Hatch). The bill would modify the affirmative commitment rules for energy tax credits and the definition of energy property eligible for the credit.

The first part is a summary of the bill. This is followed in the second part by a more detailed description of the bill, including present law, explanation of provisions, and the effective date.

I. SUMMARY

In general, the 10-percent business energy investment tax credit expired after 1982 (general 10-percent energy credit). However, the general 10-percent energy credit for certain types of long-term energy projects continues through 1990 if certain affirmative commitments have been made in connection with the projects. Also, certain business energy credits (other than the general 10-percent energy credit), such as the 15-percent credit for solar, wind or geothermal property and the 10-percent credit for biomass property, continue through 1985.

Under S. 1396, the present law affirmative commitment rule applicable to the general 10-percent energy credit would be modified for synthetic fuel production, coal conversion equipment and certain related equipment. Under this modified affirmative commitment rule, the general 10-percent energy credit for this property would be extended through 1992. The present law affirmative commitment rule (as modified by the bill) would be made applicable to chlor-alkali electrolytic cells. In addition, a special affirmative commitment rule would be created for solar, wind, geothermal, and biomass property. If the affirmative commitment requirements imposed by the bill for this property are met, the credits for these types of property would be extended through 1992.

The bill would modify the definition of shale oil equipment and synthetic fuel production equipment, and coal conversion equipment. The bill also would add tar sands property as an item of property eligible for the general 10-percent energy credit and the modified affirmative commitment rule for that credit.

II. DESCRIPTION OF THE BILL

A. Present Law

1. Overview of energy investment tax credits

Prior to 1983, a 10-percent energy investment tax credit was allowed for certain types of energy property (general 10-percent energy credit). The general 10-percent energy credit expired for these types of energy property after 1982, except that this credit applies through 1990 for long-term projects for which certain timely affirmative commitments are made (affirmative commitment rule). Property eligible for the general 10-percent energy credit under the affirmative commitment rule includes alternative energy property, specially defined energy property, recycling equipment, shale oil equipment, equipment for producing natural gas from geopressured brine, and cogeneration equipment.

In addition, a 15-percent energy credit is allowed through 1985 for solar, wind, geothermal, and ocean thermal property. Qualified intercity buses and biomass property are eligible for a 10-percent energy credit. In 1982, a 10-percent credit was added for periods beginning on January 1, 1980, and ending on December 31, 1982, for chlor-alkali electrolytic cells (P.L. 97-424). No affirmative commitment rule applies for these properties. Qualified hydroelectric generating property is eligible for an 11-percent energy credit through 1985. The credit for hydroelectric property is allowed through 1988 under a special affirmative commitment rule.

If energy property also qualifies for the regular investment tax credit, both the regular and energy credits apply. The regular investment credit for any taxable year may not exceed the lesser of the tax liability for the taxable year or $25,000 plus 85 percent of the excess of tax liability over $25,000. The energy credit may be used to offset 100 percent of tax liability after application of the regular credits. Unused credits may be carried back or carried over to other taxable years.

2. Energy credit affirmative commitment rules

General 10-percent energy credit.—Under an affirmative commitment rule, the general 10-percent energy credit (which otherwise expired at the end of 1982) applies through 1990. To qualify, the property must be part of a project with a normal construction period of two or more years. In addition, (1) before 1983, all engineering studies in connection with commencement of construction of the property must have been completed, and all environmental and construction permits required in connection with the commencement of construction must have been applied for, and (2) before 1986, the taxpayer must enter into binding contracts for the acquisition, construction, reconstruction, or erection of equipment

specially designed for the project reasonably estimated to cost at least 50 percent of the aggregate cost of all specially designed equipment for the project to be placed in service as part of the project.

Hydroelectric generating equipment.—The 11-percent energy credit for qualified hydroelectric generating equipment (which otherwise expires after 1985) applies through 1988, if an application has been docketed by the Federal Energy Regulatory Commission by January 1, 1986.

3. Shale oil equipment

Shale oil equipment eligible under the affirmative commitment rule for the general 10-percent energy credit generally means equipment for producing or extracting oil from oil-bearing shale rock. Prior to 1981, the credit did not apply to any equipment used for hydrogenation, refining, or other processes subsequent to retorting. However, for periods after 1980, the credit applies to equipment for hydrogenation or other processes applied in the vicinity of the property from which the shale was extracted and applied to bring the shale oil to a grade and quality suitable for transportation to and processing in a refinery (P.L. 97-362).

4. Synthetic fuel production and coal conversion equipment

The definition of alternative energy property eligible for the general 10-percent credit (and the affirmative commitment rule) includes equipment for converting an alternate substance into a synthetic liquid, gaseous, or solid fuel and certain coal conversion equipment. Under Treasury regulations (secs. 1.48-9(c)(5) and (7)), eligible equipment does not include equipment, such as an oxygen plant, that is not directly involved in the treatment of an alternate substance, but produces a substance that is, like the alternate substance, a basic feedstock or catalyst used in the conversion process.

B. Explanation of S. 1396

1. Overview

Under the bill, the energy credit affirmative commitment rules would be expanded and the definition of energy property would be modified for synthetic fuel production and coal conversion equipment. Tar sands property would be added as energy property eligible for the general 10-percent energy credit and the affirmative commitment rule.

2. Energy credit affirmative commitment rules

Solar, wind, geothermal, and biomass energy property.—The bill would add a new affirmative commitment rule for solar, wind, geothermal, and biomass energy property, the energy credits for which otherwise expired under present law at the end of 1985. Under the affirmative commitment rule, which differs significantly from the present law affirmative commitment rule for the general 10-percent energy credit, the energy investment credit would be available for this type of energy property through December 31, 1992.

To qualify for this affirmative commitment rule, on or before January 1, 1986, the taxpayer or any other person must have com-

pleted all feasibility studies in connection with the commencement of construction of the project, and must have applied for all environmental and construction permits required in connection with the commencement of construction of the project. This rule would modify the present law affirmative commitment rule by substituting a requirement of completion of feasibility studies for the requirement of completion of engineering studies.

In addition, on or before January 1, 1988, the taxpayer must have entered into binding contracts for the acquisition, construction, reconstruction, or erection of (1) equipment for the project (whether or not specially designed equipment) reasonably estimated to cost 50 percent of the aggregate cost of all equipment to be placed in service as part of the project upon its completion, or (2) equipment specially designed for the project reasonably estimated to cost at least 50 percent of the aggregate cost of all specially designed equipment for the project to be placed in service as part of the project upon its completion. This rule would modify the parallel provision under the present law affirmative commitment rule by adding item (1) above as a means of meeting the requirement.

Unlike the present law affirmative commitment rule, there would be no requirement that the project have a normal construction of two years or more.

Synthetic fuel production and coal conversion equipment.—The bill would modify the present law affirmative commitment rule applicable to the general 10-percent energy credit for synthetic fuel production equipment, coal conversion equipment, and related pollution control or handling equipment by (1) extending the termination date for the credits under the affirmative commitment rule from December 31, 1990 to December 31, 1992, and (2) substituting June 30, 1987, for the January 1, 1983, date, relating to completion of engineering studies and application for permits, and (3) substituting December 31, 1988 (or, if later, 18 months after commencement of construction of the project) for the January 1, 1986 date, relating to binding contracts for specially designed equipment.

Chlor-alkali equipment.—The present law affirmative commitment rule applicable to the 10-percent general energy credit (without the modifications described above for synthetic fuel production and coal conversion equipment) would be made applicable under the bill to chlor-alkali electrolytic equipment.

3. Tar sands property

Under the bill, tar sands property would be made eligible for the general 10-percent energy credit and the affirmative commitment rule for that credit. Tar sands property would be defined as equipment necessary and integral to mining, quarrying, or extraction of tar sands, or to the production or extraction of oil from tar sands. Eligible equipment would include equipment used for cracking, coking, hydrogenation, or similar process, but would not include any equipment used for refining.

4. Shale oil equipment

The definition of shale oil equipment, which is eligible for the general 10-percent energy credit, would be amended in two respects. First, mining equipment would be referred to expressly as

qualifying equipment. Second, the definition of eligible property would be amended to include equipment for preprocessing shale oil (including property used for hydrogenation, denitrogenation, dearsenation, desulphurization, and deoxygenation) or for similar preprocessing, prior to processing in a conventional refinery instead of referring to hydrogenation or other processes applied in the vicinity of the property from which the shale was extracted and applied to bring the shale oil to a grade and quality suitable for transportation to and processing in a refinery.

5. Synthetic fuel production and coal conversion equipment

The bill would modify the definition of synthetic fuel production equipment and coal conversion equipment, which is eligible for the general 10-percent energy credit, to include equipment, such as an oxygen plant, that, though not directly involved in the treatment of an alternate substance, produces a basic feedstock or catalyst used in such conversion process, and other auxilary equipment.

C. Effective Date

No effective date is contained in the bill. Thus, it is unclear whether the bill is intended to apply to investments made during periods prior to the date of enactment.

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